

MEMORANDUM

FROM: Timothy White
Special Counsel
Office of the Chief Counsel, Division of Trading and Markets
U.S. Securities and Exchange Commission

RE: Meeting with representatives from crowdfunding portals

DATE: June 18, 2012

On June 18, 2012, Commission staff met with representatives from crowdfunding portals to discuss issues regarding the implementation of Title III of the Jumpstart Our Business Startups Act.

The following Commission representatives were present: David Blass, Joseph Furey, Joanne Rutkowski, Ignacio Sandoval, and Timothy White from the Division of Trading and Markets; and Lona Nallengara, Lillian Brown, and Sebastian Gomez Abero from the Division of Corporation Finance.

The following representatives from crowdfunding portals were present: Candace Klein of SoMoLend and Crowdfund Intermediary Regulatory Advocates; Luan Cox of Crowdnetic; D.J. Paul of Crowdfunder; Freeman White of Launcht; Sherwood Neiss of Startup Exemption; Chris Tyrrell of Crowd Platform; and Douglas Ellenoff and Joan Adler of Ellenoff, Grossman & Schole, LLP.

The meeting agenda provided by the crowdfunding portal representatives is attached.

Attachments



Discussion Points for Meeting
between SEC Representatives
and Crowdfunding Organization Leaders
Regarding Regulation of Funding Portals

A. Portal registration and requirements

Registration of portal with FINRA

Limited examination for investor protection and compliance of portal

Insurance

Recordkeeping

Investor records

Issuer/funding records

Multiple websites under a single portal

Bad actor exclusions

Financial responsibility

Portal

Issuer funds

FINRA examinations / oversight

Dispute resolution

B. Portal mechanics

Establish issuer parameters (no investment “qualifiers”)

Intermediary services

Due diligence

Background checks

Standard documents (business plan format, investor questionnaire,
subscription agreement)

Fees, including fees for third party services

Advertising

C. Portal investor protection

Investor qualification - investor income and investing history

Escrow for investor funds

Educational materials

Disclosure requirements (issues related to responsibility for various
disclosures)

Risk alerts

SEC directed information

Terms of use

Privacy policy

Fraud detection

D. Supplemental suggestions and considerations

Designated adviser

Broker Dealer Partnership suggestions (branch office, etc.)



The Crowdfund Investing Regulatory Advocates
20-22 W. 12th Street
Cincinnati, OH 45202
info@startupexemption.com

By Email (rule-comments@sec.gov) and U.S. Mail

June 5, 2012

U.S. Securities and Exchange Commission
100 F Street NE
Washington, D.C. 20549-1090
Attn: Ms. Elizabeth M. Murphy, Secretary

**Re: Public comments on SEC Regulatory Initiative under the JOBS Act pertaining to
General Solicitation in Titles II & Titles III**

Ladies and Gentlemen:

I am writing on behalf of the Crowdfund Intermediary Regulatory Advocates ("CfIRA"). On behalf of CfIRA, I wish to thank you for the opportunity to submit these written comments relating to the implementation of Title III of the Jumpstart Our Business Startups Act (the "Act"). In drafting rules and regulations to implement the Act, we wanted to propose certain safe-harbors that would address certain fundamental issues that have arisen with regard to the Act and to the development of the crowdfunding industry.

I. POSTING CRITERIA

A. Background: The Investment Advisers Act of 1940, as amended, defines an "investment adviser" as anyone who (i) for compensation, (ii) is engaged in the business of (iii) providing advice to others or issuing reports or analysis regarding securities.

B. Question: Is a funding portal that refuses to post the offerings of certain issuers an investment adviser?

C. Considerations: CfIRA agrees that any funding portal that directly engages in subjective evaluation of businesses for purposes of directing investors on its website to the offerings of such businesses would be engaged in the business of providing advice to others regarding securities and, as a result, should be regulated as an investment adviser. However, we do think that funding portals should be permitted to enforce objective listing criteria without being deemed to be an investment adviser. For example, we expect that certain intermediaries will solely focus on debt offerings, while others will list only equity offerings. Certain of our members have also indicated their intent to not list offerings of businesses that they find objectionable, whether from a moral or legal perspective. For example, certain portals may

refuse to list any business relating to: (i) firearms, (ii) tobacco, and (iii) sex-oriented businesses. Similarly, some of our members have indicated their intent to focus on certain size of offerings or issuers, limiting their offerings to those that either exceed or are less than a certain threshold or to issuers meeting certain metrics (i.e., valuation/EBITDA/revenue). Finally, we expect portals to focus on niche segments of the economy, such as the arts and film or socially conscious investing.

D. Conclusion: We believe that funding portals should be permitted to enforce objective and clearly disclosed listing criteria for issuers without being deemed to be investment advisers. In practice, the safe-harbor should be relatively broad, allowing for niche funding portals (for example, portals that focus solely on the film-making industry) to develop as the crowdfunding industry develops.

E. Proposed Safe-Harbor: Any funding portal that refuses to list or sell the securities of an issuer, or that only lists or sells the securities of certain issuers, in each case as a result of objective and clearly disclosed listing criteria, shall not be deemed, as a result of the promulgation and enforcement of such criteria, to be an investment adviser within the meaning of Section 202(a)(11) of the Investment Advisers Act of 1940, as amended.

II. FRAUD AND RISK OF FRAUD

A. Background: The Investment Advisers Act of 1940, as amended, defines an “investment adviser” as anyone who (i) for compensation, (ii) is engaged in the business of (iii) providing advice to others or issuing reports or analysis regarding securities.

B. Question: Is a funding portal that refuses to post the offerings of certain issuers an investment adviser?

C. Considerations: Part of the rationale behind crowdfunding is the “intelligence of the crowd,” and incidences of fraud are discovered by the crowd on existing crowdfunding platforms not involving the sale of securities.¹ Additionally, it is expected that intermediaries, whether through their own diligence efforts, the due diligence of third-party service providers, and/or the diligence of crowd vetting will discover certain indicia of fraud or potentially fraudulent activity.

D. Conclusion: The Act in no way mandates that intermediaries list or sell the stock of all issuer that desire to use the services of said intermediary. In fact, the Act requires intermediaries to take measures to reduce the risk of fraud. We believe that funding portals should have the ability to refuse to list or sell the securities of an issuer, or remove an existing listing of an issuer, if the funding portal has some reasonable basis for believing that an offering or those participating in an offering may be fraudulent or presents a heightened risk of fraud to investors.

F. Proposed Safe-Harbor: Any funding portal that refuses to list or sell the securities of an issuer, or cancels a listed offering, because such funding portal suspects, with or

¹ For example, please see: <http://betabeat.com/2012/04/this-is-what-a-kickstarter-scam-looks-like/>

without evidence, that an offering may be fraudulent or presents a risk of fraud to investors shall not be deemed, as a result of such refusal, to be an investment adviser within the meaning of Section 202(a)(11) of the Investment Advisers Act of 1940, as amended.

III. CROWD COMMENTARY

A. Background: The power of crowdfunding is, in part, based on its strong connection with social media. In our view, the success of crowdfunding will be based upon the quick and efficient exchange of information. As stated above, the crowd is powerful at discovering fraud. However, we also expect crowd interaction with entrepreneurs to be a powerful factor in building strong companies, offering suggestions on improving businesses and products. We expect this information to consist of objective analysis and subjective thoughts and concerns about an offering, and we believe each is appropriate to be exchanged between investors. We highly suggest the staff review the interaction on existing crowdfunding (non-security) sites, such as www.kickstarter.com, to discover how powerful these exchanges of information can be.

B. Question: May a funding portal host discussion boards and other interactive information exchanges?

C. Considerations: The reality is, whether hosted on a funding portal's site or not, the crowd is going to exchange information about offerings via social media and their social networks. Once information exists on the internet, there is no way for a funding portal or for an issuer to control or limit the spread of such information. Given this expectation, we suggest it would be most efficient to host such informational exchanges and message boards on the funding portal's site. In this way, investors can share information, and ask questions of issuers. In short, the crowd will vet and discuss the issuers and their businesses. Issuers can respond and interact with their investors (and potential investors), and learn more about their products and prospects.

D. Conclusion: Information will be exchanged about issuers, the only question is where. For a variety of reasons, including encouraging a transparent crowdfunding marketplace, we believe that funding portals should be permitted to host message boards and other information exchanges. Importantly, by hosting informational exchanges, the portals will be helping to avoid asymmetry of information, as a centralized location for information should provide a mechanism for the open and transparent exchange of information.

E. Proposed Safe-Harbor: A funding portal which hosts discussion panels and other mediums for the exchange of information between investors and issuers shall not be required to register as a broker or dealer under Section 15(a)(1) of the Securities Exchange Act of 1934, as amended, and shall not be deemed to be an investment adviser within the meaning of Section 202(a)(11) of the Investment Advisers Act of 1940, as amended, so long as the funding portal, its officers, directors, and employees, do not participate (other than moderating discussions and removing postings that are abusive) in such discussion forums other than to enforce clearly disclosed rules regarding posting and the exchange of information.

V. PEER-TO-PEER LENDING

A. Background: Obviously, crowdfunding can take many forms. However, we would posit that when most people think of crowdfunding, they think of equity crowdfunding. In fact, however, debt crowdfunding, or peer-to-peer lending, is probably going to be the most utilized crowdfunding capital raising mechanism in the small business space. The reasons are two-fold. First, “idea” or growth companies are more likely to need to use “equity” returns to entice investors. These early-stage businesses fail at a high rate, and investors will need to be compensated for taking this risk. Existing small businesses, however, present a completely different investment opportunity. First, existing businesses will have been in business for some period of time. Second, these businesses will have (i) financial records, (ii) a credit history and (iii) cash flow. As a result of these attributes, investors will be willing to accept a more limited return, as the investment will be less risky. The issue with peer-to-peer lending is, of course, that someone has to set an interest rate. Given the various attributes of a business, what is the risk of that loan defaulting and, as a result, what interest rate should be charged to compensate for that risk? Early in the history of the two existing peer-to-peer lending institutions, Prosper and LendingClub, the “auction” process was utilized. In effect, borrowers set the interest rate and lenders decided whether or not to invest. From what we understand, the auction model was not successful because the interest rates were tied to the popularity of the offering rather than objective measures of credit risk. In effect, “ideas” were being funded at interest rates that did not compensate the investors for objective credit risk, defaults were high and the system was abandoned. Both Prosper and LendingClub have moved to the underwriting model, where objective criteria are used to create a credit rating and the interest rate charged on a loan are based on that credit rating.

B. Question: Is a funding portal that uses objective criteria to set interest rates acting as an investment adviser?

C. Considerations:

a. Security: in an equity crowdfunding raise, investors will most likely purchase common stock, which is the last to get paid. On the other hand, a peer-to-peer investor will have a security that is paid prior to any equity security (including preferred stock). In addition, unlike equity offerings, which may not require the payment of dividends and are not required to explain the process for the return of capital, debt securities will have set maturity dates and a clear process to liquidity. Investors are by definition purchasing a “safer,” security in the peer-to-peer lending arena, with a clearer liquidity path.

b. Objective criteria: we agree that subjective underwriting is an activity that is best regulated under the broker/dealer or investment adviser laws. However, it is also true that there are objective measures of credit risk. Quite simply, the less time a business has been operating, the more likely that a loan to that business is to default. Similarly, the higher the debt/equity ratio, the more likely a loan is to default. An objective underwriting process will result in such loans with these characteristics paying a higher interest rate – compensating (and thus protecting) investors from this risk.

c. Cost: our members have no intent to advise investors on the advisability of purchasing any security and, therefore, plan to limit their underwriting solely to applying their objective criteria of credit risk. By mandating registration under the broker/dealer and/or investment adviser rules, the cost of such registration will be passed on to issuers and investors with no tangible benefits to either.

d. Small businesses: the cost of registration will also be placed on the segment of crowdfunding least able to accept such costs. The average commercial peer-to-peer loan is \$18,000. If peer-to-peer intermediaries are required to register as a broker/dealer and/or investment adviser, it will be forced to pass on that cost to issuers/investors. Doing so will raise the cost of raising capital on the segment of our economy that currently faces the biggest hurdles raising capital – small businesses.² This incremental cost increase will make peer-to-peer lending inefficient at best, and could even be fatal to peer-to-peer lending.

D. Conclusion: We believe that interest rates can be set by objective criteria. We understand, however, that there is a fine line between providing objective underwriting and providing objective and subjective investment advice. We think the combination of (i) disclosure and (ii) investor education can be used to address these concerns.

E. Proposed Safe-Harbor: A funding portal which engages in underwriting activities for the purpose of setting interest rates for debt instruments which are to be sold or offered for sale by such intermediary shall not be required to register as a broker or dealer under Section 15(a)(1) of the Securities Exchange Act of 1934, as amended, and shall not be deemed to be an investment adviser within the meaning of Section 202(a)(11) of the Investment Advisers Act of 1940, as amended, so long as:

a. the underwriting is based upon objective criteria such as years in business, credit score, loan-to-asset ratios and debt-to-income ratios;

b. the funding portal prominently discloses that it does limited underwriting, solely for the purposes of setting interest rates, based on objective information provided by the issuer; and

c. The funding portal holds itself out as a listing or matching service and not as providing any other securities-related services except for the limited underwriting discussed above.

² We believe that “idea” and early-stage companies are most likely going to be required to issue equity, as investors will demand unlimited upside for the significant risk of investing in early-stage companies. On the other hand, existing small businesses will gravitate toward debt instruments, which will have a fixed rate of interest and known maturity date.

VII. MATCHING

A. Background: We anticipate that funding portals will provide search and other information management tools so that investors can focus their efforts on companies that meet certain criteria. So, for example, we anticipate that an investor will be able to search by industry, years in business, size of business (whether by revenue or some measure of profitability), size of offering, number of investors, average size of investment, geographic location and percentage of offering funded. We also anticipate that the portals will notify investors when companies meeting their criteria register with the funding portal.

B. Question: Can a funding portal provide search and information management tools to investors, and provide notices to investors when companies meeting their criteria register with such portal?

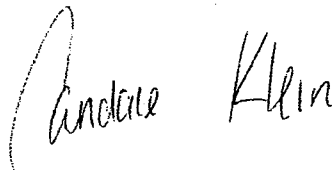
C. Considerations: As indicated elsewhere in this letter, we expect social media and social networks to play a huge role in the success of crowdfunding. As can be seen by the success of crowdfunding on existing platforms (non-security), investors want to invest in their communities, whether that is geographically based or, instead, based on some other criteria (such as industry). While we do expect niche crowdfunding sites to develop, we also expect that generalized sites will provide information management tools so that investors can find businesses meeting their criteria for investment. Such tools will permit investors to more easily find companies meeting their investment criteria.

D. Conclusion: A portal that provides information management tools, such as search functions and automatic notification mechanism, should not be deemed to be acting as an investment adviser.

E. Proposed Safe-Harbor: A funding portal which provides information management, search and automatic notification tools shall not be required to register as a broker or dealer under Section 15(a)(1) of the Securities Exchange Act of 1934, as amended, and shall not be deemed to be an investment adviser within the meaning of Section 202(a)(11) of the Investment Advisers Act of 1940, as amended, so long as such tools are based solely on objective criteria (such as industry, years in business, size of business (whether by revenue or some measure of profitability), size of offering, geographic location and percentage of offering funded) and the funding portal holds itself out as a listing or matching service and not as providing any other securities-related services.

We are available to further discuss the recommendations and concerns expressed in this letter. We further expect to provide additional safe-harbor requests in the future, as we have several working groups gathering information on what "best practices" can be developed to serve issuers and investors alike. We look forward to supporting the work of the Staff over the course of the next few months and to making crowdfunding a success for investors, small business and entrepreneurs.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Candace Klein". The signature is fluid and cursive, with the first name "Candace" written in a larger, more prominent script than the last name "Klein".

Candace Klein
Founder & CEO, SoMoLend

A handwritten signature in black ink, appearing to read "Vince Molinari". The signature is very stylized and cursive, with the first name "Vince" being the most prominent part of the signature.

Vince Molinari
Founder & CEO, GATE Technologies

CFIRA's Official Position on JOBS Act with the SEC

On May 22, 2012, the Crowdfunding Intermediary Regulatory Advocates submitted the following position paper to the Security and Exchange Commission.



U.S. Securities and Exchange Commission
100 F Street North East
Washington, DC 20549

RE: SEC Regulatory Initiatives
JOBS Act Title III: Crowdfunding Exemption
Ladies and Gentlemen:

We are the Crowdfunding Intermediary Regulatory Advocates ("CFIRA"). We wish to thank you for the opportunity to meet with certain Securities and Exchange Commission ("SEC") representatives on April 20, 2012 to discuss a variety of issues related to the implementation of Title III of the Jumpstart Our Business Startups Act (the "Act"). CFIRA is a coalition comprised of certain of the crowdfunding industry's leading intermediary platforms and experts actively participating in the crowdfunding industry. Our mission is to facilitate capital formation by creating an equitable, orderly and vibrant crowdfunding market that inspires investor confidence and encourages participation by small businesses and new ventures.

On April 20, 2012, representatives from our organization attended a meeting with certain members of the Corporate Finance Division, Trading and Markets Division and Office of the Compliance Inspection Division of the SEC (the "Staff") to discuss the new rules and regulations governing crowdfunding to be implemented pursuant to the Act. The meeting was a productive starting point as both the Staff and industry members shared their views of how best to fashion a new regulatory regime tailored to this evolving and rapidly expanding industry.

We respectfully submit the following comments and summarize the views expressed at the meeting with the Staff, along with our comments to certain

other provisions of the Act.

We have also included as an attachment to this letter a copy of a letter we are sending to the White House regarding the continued applicability of the general solicitation rules in the context of a Rule 506 private placement.

I. Investor Protection

We believe the success of crowdfunding will be dependent upon recognition of the power, influence and opportunity afforded to entrepreneurs by new media technology and the creation of a comprehensive regulatory framework which protects investors from potential harm. We seek to work with the Staff to develop a system which includes transparency, "crowd-intelligence" and common sense oversight enacted in such a manner that preserves the integrity and scalability of internet-based platforms envisioned by the Act. At the April 20, 2012 meeting, several notable and experienced representatives from internet sites, or "portals," presented a number of infrastructure models and computing and fraud detection systems currently employed in the donation-based rewards-based markets. These models, some of which are discussed in greater detail below, along with models from other business marketplaces and exchanges, should be supplemented by additional investor protections, including a portal registry and unique URL's for such portals, a background and securities enforcement history check of the officers and directors of the issuer and the portals, required investor education and certain investor due diligence requirements.

a. Infrastructure Models and Computing and Fraud Deterrence and Detection Systems

Section 302(b) of the Act requires crowdfunding intermediaries to implement measures to reduce the risk of fraud. The Act does not mandate the infrastructure that intermediaries must implement in creating their portals. Intermediaries will require a degree of freedom in developing their portals in order to differentiate themselves from one another. That said, we believe the infrastructure utilized by each intermediary should incorporate some type of fraud deterrence and fraud detection system, whether proprietary or licensed through a third party provider. In terms of fraud deterrence, we believe portals should have a video interface whereby each issuer is required to give a short presentation on their business which is capable of being viewed live and saved for later viewing at any time by a potential investor. This will not only help to deter fraud, but it will also enable potential investors to get to know the person with whom he or she is investing. In addition, we believe the SEC should adopt a provision requiring the wiring of the net proceeds from funded offerings to a corporate entity in the US. This will deter fraud from foreign issuers looking to take advantage of the Act's money raising capabilities without being subject to US securities laws.

The SEC should also require intermediaries to build certain fraud detection systems into the functionality of their portal. For example, the SEC should

require intermediaries to have a simple "checks and balances" system whereby the portals run a weekly data analysis on a search engine in order to compare the due diligence that was conducted prior to the issuer's posting with any news on the issuer or its officers and directors that has occurred subsequently.

b. Portal Registration

In addition to the protections offered by the portals themselves, we respectfully suggest the Staff consider the creation of a Registered Portal-Check, similar to the Broker-Check system maintained by the Financial Industry Regulatory Authority ("FINRA"). The register will serve to protect both issuers and investors from the risks of unregistered intermediaries and provide greater transparency for all crowdfunding participants. We recommend this system clearly identify the registration status of a funding portal and its management, display any regulatory actions against such portal, and provide a hyperlink to its website. This will provide investors and issuers with an opportunity to easily confirm the registration status of an intermediary site.

c. Due Diligence Requirements With Respect to Issuers

Section 4(a)(5) of the Act requires intermediaries obtain a background and securities enforcement regulatory history check on each officer, director and person holding more than 20 percent of the outstanding equity of every issuer whose securities are offered. However, the Act does not address the extent to which an intermediary must delve into the background of an issuer or how thorough the background check must be. This has the potential to create a barrier to entry restricting opportunities of issuers and intermediaries to adequately protect investors and raise funds. We believe the scale of such background checks should be related to the size of the transaction, while also establishing a minimum requirement that is an effective mechanism against fraud. We believe the SEC should establish a minimum level of diligence an intermediary must undertake in order to facilitate the sale of an issuer's securities and that such minimum level be below the current requirements for broker-dealers undertaking private placement offerings.

As the Staff considers the scope of the due diligence required by the Act and balances the need to protect investors and the costs of compliance, we emphasize the separate and distinct obligations that should be applicable to funding portals and brokers. Although FINRA has provided its members with guidance on its due diligence obligations in the context of private placements, we note that, unlike broker-dealers, funding portals have a more limited role in the crowdfunding securities transaction, and are subject to greater limitations. Such limitations include a prohibition on providing investment advice or recommendations regarding specific issuers and the amount able to be invested by individual investors. We believe the scope of due diligence required of portals should be limited to conducting a commercially reasonable investigation based upon information publicly available on the SEC and FINRA websites (as well as the website of the self-regulatory organization which will have ultimate oversight of the crowdfunding industry), issuer

questionnaires and negative assurances from the issuers' related parties. Again, we believe it most helpful if the Staff provides a safe harbor on what searches and background checks will satisfy this requirement.

11. Securities Offered Through Portals and Financing Mechanics

We believe the Staff should expressly confirm the current language in the Act that any form of equity or debenture security, as well as those convertible or exchangeable for other securities, may be sold pursuant to the Act. A broad spectrum of securities will help to create a more vibrant and useful crowdfunding marketplace. We believe investors can be adequately protected by requiring intermediaries to include a glossary explaining each type of security available for purchase in each of the offerings on its portal.

We accept the Staff's position, which is consistent with historic practice, that a registered investment funding portal which is not duly registered as a broker-dealer should not be permitted to hold funds and that a third-party should be engaged for such purpose.

III. Advertisements and Investment Advice a. Advertisements

The ability of an issuer and an intermediary to utilize new media technology to generate interest in itself is critical to the success of crowdfunding and can be appropriately balanced with necessary investor protection. Section 302 of the Act expressly prohibits intermediaries from compensating promoters, finders or lead generators for providing the intermediary with the personal identifying information of any potential investor. We would appreciate clarification from the Staff concerning other ways companies can currently generate lists of investors and the myriad of ways to reach them and whether such approaches would conflict with the Staff's concern on general solicitation. The Staff emphasized in its reading of Section 4A of the Act that issuers were prohibited from soliciting investors and that portals may market and advertise to promote the portal itself to attract investors, but may not advertise the terms of any specific offering. We believe clarification should be issued that a portal is allowed to advertise that certain issuers are utilizing their portal without providing any of the terms of a particular offering, should be able to advertise offerings just listed, offerings that were successfully funded (similar to the current broker-dealer practice of utilizing tombstones) and the number of investors in a recently closed offering. Furthermore, issuers should be able to promote their offering through their own platform as long as all such notices include a link directly to the registered intermediary.

b. Investment Advice

The Staff's interpretation of what constitutes investment advice under the Act is an issue of primary importance to intermediaries. The Act clearly forbids an intermediary from providing investment advice or recommendations whether to invest in a security. However, the Act becomes less transparent when considering, for example, if an intermediary's decision to work with a particular issuer instead of another (whether based upon industry, product,

moral or ethical considerations or use of proceeds) constitutes investment advice. CFIRA hopes the Staff will establish bright lines making it clear how an intermediary maintains its independence and avoids being deemed to be giving investment advice.

Intennediaries need the ability to make judgments about issuers within certain parameters, as well as the flexibility to revise those parameters as their own businesses evolve, without having to host every entrepreneur hoping to raise money. P01tals must be pennitted to be selective in which issuers they permit to sell securities on their intetface. We believe such freedom is not only consistent with the intent of Congress, but that it will also augment investor protections as it creates another sow'ce through which issuers are vetted prior to raising money from the public.

The need for intennediary discretion without offering investment advice can be satisfied in a few ways. First, require intennediaries to enact and publish pre-established guidelines, tenns and conditions setting forth the requirements and processes by which issuers are selected to sell securities through their site. These guidelines may be based on industry, size of company or any other parameters an inte1mediary chooses to establish. Intetmediaries should publish on their websites a disclaimer that its selection or rejection of an issuer does not constitute investment advice. Those guidelines should include the ability to discontinue an issuer's offering based on parameters established in such guidelines. Intennediaries need the ability to modify these parameters in their own business judgment, but such modifications must have been enacted by management consent of such intermediary not less than 30 days prior to such portal offering any investment under such new parameters. Second, provide clear disclosure to, and require express acknowledgement from, investors of the then-existing guidelines.

Although prohibited from giving investment advice, intetmediaries will need the

flexibility to distinguish themselves from one another in order to compete for issuers and investors. Ways they may seek to accomplish this include by industry, geography and size of company, but will almost certainly include the design and navigability of their site, access by issuers and investors to infonnation about current market conditions and str uctures of recent deals (whether within a particular industry or in the crowdfunding industry in general) and the look and feel of an issuer presentation (a portal may detennine that all issuer presentations must confohn to a certain style and may even help with the preparation and editing of such infonnation). We hope the Staff makes it clear that intennediaries will have this flexibility as their business needs evolve and that any such variation will not, in and of itself, constitute advice with respect to a pruticular investment.

IV. Know Your Crowd and Investor Due Diligence

The Act requires intennediaries to educate investors on the risks associated with crowdfunding securities and ensure that such investors demonstrate an

understanding of such risks. Sections 4(a)(3) and 4(a)(4) of the Act require intermediaries to provide certain disclosures relating to risks and other "investor education materials" to investors and ensure that such investors understand them. We agree investors should demonstrate an understanding of and expressly acknowledge, the risks inherent in investing in new ventures and small businesses, as well as the liquidity risks of owning unregistered securities. However, there is ambiguity in the Act which we believe requires clarification from the Staff. For example, the Act does not properly define "investor education materials," nor does the Act contemplate the frequency with which intermediaries must educate investors or the certainty with which intermediaries must ensure the investors have been educated. The intermediary will control the means by which an investor's knowledge is checked, but at a minimum, the intermediary should demonstrate that a reasonable person had the opportunity to learn and understand the basics of making an investment of this nature. The intermediary should not be required to educate an investor each time they invest, but every twelve months, an investor should be required to re-enroll in the educational program. The intermediary should be required to update its educational materials as and when appropriate. To ensure an investor understands the educational materials, the investor should affirm via digital signature that he or she understands the educational materials prior to investment. We believe intermediaries should also be required to include a glossary explaining each type of security available for purchase in each of the offerings on the platform. This will put the investor in a more favorable position to make an informed investment decision. It would be most helpful if the Staff provides a safe harbor on what will satisfy these requirements.

Section 302 of the Act establishes investment limits for investors based upon a percentage of such investors' annual income or net worth. This restriction protects investors from overconcentration in a single issuer and the potential risk of loss associated with new ventures. We believe it is Congress' intent to protect unaccredited retail investors and we urge the Staff to expressly distinguish between retail and institutional investors and accredited and unaccredited investors in the sale of securities, as it does in other securities transactions. The new regulations should exclude institutional and accredited investors from the definition of "person", thereby permitting institutions and accredited investors to invest in excess of \$100,000 in any one issuer. Institutional investors have the requisite experience, and both institutional and accredited investors have greater access to resources to conduct comprehensive due diligence and the ability to better manage risk of loss, than an unaccredited retail investor. This key interpretation will provide small businesses and new ventures greater access to capital through a more limited shareholder base. The regulations should also expressly permit crowdfunding funds, provided the sponsors of such funds are responsible for verifying the income or net worth level of their investors in accordance with the

requirements set forth in the Act.

In connection with investing in private placement transactions, FINRA currently permits its registered members to confirm a person's status as an "accredited investor" by completing an investor questionnaire. Current regulations do not require further due diligence to confirm, absent actual knowledge of fraud, a person's annual income or whether any other "accredited investor" threshold has been properly satisfied. We believe the imposition of any greater due diligence obligation on a crowdfunding intermediary would be impractical and unwarranted. It also seems impractical to require an intermediary to confirm whether an investor has participated in prior crowdfunding offers on other portals and the extent of any single investor's crowdfunding investments. We respectfully request the Staff clarify that the burden on establishing the accredited status of any investor be to obtain various representations and warranties from the investor, including with respect to any other crowdfunding investments made and that such investor meets the minimum income requirements required by the Act. The Staff should further clarify that an intermediary can only confirm investor compliance with the investment limitations of Section 302 of the Act solely with respect to other crowdfunding investments made through that same intermediary.

V. Crowdfunding and Integration Doctrine

Section 302(a) of the Act permits issuers to sell up to an aggregate of \$1,000,000 of its securities during any 12 month period. Section 4A(g) of the Act states that an issuer is not restricted from raising capital by methods other than crowdfunding, and that businesses may also seek to raise additional capital prior to, concurrently with or subsequent to a crowdfunding offering through a private placement (for example, pursuant to a Rule 506 offering). It therefore suggests that the two offerings are mutually exclusive and should not be subject to the integration doctrine. We respectfully request the implementing rules state clearly that a Rule 506 offering and a crowdfunded offering will never be integrated except under narrow, specifically defined circumstances.

VI. Guidance on Issuer Disclosure

It is a core principal of our regulatory system that investors have equal access to full disclosure of all material information concerning an issuer. The Act requires issuers to provide certain information to investors including, but not limited to, its management structure, business plan, offering amount, capital structure, method of valuing its securities and risk disclosures. To facilitate full disclosure, we respectfully request the Staff provide a form disclosure document for issuers which simplifies the process and provides legal certainty for investors, intermediaries and issuers.

We also note that Section 4A(c) of the Act provides for Section 12(a) liability for material misstatements and omissions. We respectfully suggest that an anti-fraud standard would be more appropriate in this context, since the disclosure requirements under the Act are less than those required in a prospectus filed

pursuant to the Securities Act of 1933, as amended.

VII. Crowdfunding Investors and Held of Record Calculation

The Act provides that securities sold in crowdfunding offerings are exempt from the "held of record" calculation in connection with the registration requirements under Section 12(g) of the Securities Exchange Act of 1934, as amended ("Section 12(g)"). Investors who purchase securities in a crowdfunded offering will be restricted from transferring these securities for a period of one year. The Staff has taken the position that the exclusion from the "held of record" calculation attaches to the holder and not the security. Therefore, upon expiration of the one year transfer period and a subsequent transfer by the initial investor, the new shareholder will be included in the "held of record" calculation. Such transfers may trigger the registration requirements of Section 12(g), which will require the issuer to expend valuable time and money to register with the SEC. For small business and startup ventures, this registration requirement could decimate an issuer's working capital and cause irreparable damage to its business

and operating prospects. Such a requirement would also seriously hamper efforts to make crowdfunding a practical, long-term alternative for the investment community. The need for additional capital to meet registration requirements will result in either an issuer borrowing money, thus leveraging its business, or raising additional capital through a subsequent equity offering that will unnecessarily dilute existing stockholders. We respectfully request the Staff either state clearly that the "held of record" calculation attaches to the security and not the holder or extend the exclusion for a period of time well beyond one year.

VIII. Audit Requirements

Under the Act the extent to which an issuer must disclose its financial statements varies depending on the aggregate amount offered, including any prior offerings in the preceding 12 month period. For crowdfunded offerings with an aggregate offering amount up to \$100,000, the issuer must disclose its most recently filed income tax returns and its financial statements certified by the issuer's principal executive officer. For offerings that exceed \$100,000 during any 12 month period but are less than \$500,000, the issuer must provide financial statements reviewed by an independent public accountant. If an aggregate offering amount exceeds \$500,000, the issuer must provide audited financial statements. The Act permits the SEC to establish rules amending the \$500,000 threshold requiring audited financial statements.

As the Staff is aware, preparing audited financial statements is a costly, time-consuming process not required of similarly situated private companies raising money under current SEC regulations. We see no reason for a more onerous

burden on companies seeking capital through crowdfunding, as this would be a primary obstacle frustrating efforts to raise money pursuant to the Act and a substantial hurdle for the industry as a whole to overcome. We respectfully request the Staff consider the totality of the costs of meeting the foregoing obligations on the issuer, as well as the harmful impact on the nascent crowdfunding industry, and apply the requirement to provide audited financial statements solely to issuers which have been engaged in their current business for more than 12 months and which are seeking to raise at least \$1,000,000. Companies in existence for less than 12 months should further be exempt from providing independently certified financial statements. Such issuers (and perhaps even the intermediaries) should be required to make appropriate disclosure regarding the lack of operating history, the absence of revenue and the unavailability of reviewed financial statements.

Further, we would appreciate clarification from the Staff whether a crowd-funded offering will be considered, for the purposes of the audit provisions, to be "public," and thus the Generally Accepted Auditing Standards for such an audit will be under the jurisdiction of the PCAOB, or "private" and under the jurisdiction of the ASB (Audit Standards Board). Due to the relative size and nature of crowd-funded offerings, we believe the financial statements should be under the jurisdiction of the ASB, not the PCAOB.

IX. Registration and Self Regulatory Organization

FINRA vs. NFA – Group to discuss.

X. Recommended Timeline

The Act requires the SEC to adopt the final regulatory regime for crowdfunding within a maximum of 270 days of its enactment. We commend the SEC on its prompt action and consultation with members of our industry. In an effort to continue to build on the constructive relationship that has developed between our organizations and to ensure Congress' timetable is respected, we respectfully propose working together in accordance with the following timetable to ensure this limited rule making period is both productive and comprehensive.

We have identified the following issues in order of primacy that we will be analyzing and wish to simultaneously work with you to prepare:

- May - Investor Protection, Due Diligence, Fraud Deterrence and Detection
- June - Advertising and Investment Advice
- July- Registration Process and Self-Regulatory Organization
- August – Disclosure Requirements and Offering Memoranda
- September- Crowdfunding Mechanics
- October- December: Concurrent Period on Draft Regulations and Adoption
- January 1, 2013- Crowdfunding Launch Date!

The members of the Crowdfunding Advisory Group of CFIRA remain avail

able to further discuss the recommendations and concerns expressed in this letter. We look forward to supporting the work of the Staff over the course of the next few months as well as in the future, and to making this program a success for investors, small business and entrepreneurs.

Respectfully submitted,

Candace S Klein, Chair, CFIRA

Vincent R Molinari, Co-Chair, CFIRA